Supreme Court, U.S.
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No. 91-1695

IN THE

Supreme Court of the United States

OCTOBER TERM, 1992

PIONEER INVESTMENT SERVICES COMPANY,
Petitioner,

v.

BRUNSWICK ASSOCIATES LIMITED PARTNERSHIP, CLINTON ASSOCIATES LIMITED PARTNERSHIP, FT. OGLETHORPE ASSOCIATES LIMITED PARTNERSHIP, AND WEST KNOXVILLE ASSOCIATES LIMITED PARTNERSHIP,
Respondents.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

BRIEF FOR RESPONDENTS

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RESTATEMENT OF QUESTION PRESENTED

Whether Respondents may file proofs of claim in a chapter 11 case a mere 20 days after the "bar date" because of "excusable neglect" as defined in Bankruptcy Rule 9006(b)(1), where the delay in filing was not in bad faith and neither prejudices the debtor nor adversely impacts administration of the case.

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BRIEF FOR RESPONDENTS

STATEMENT OF THE CASE

On April 12, 1989, Petitioner filed for reorganization under chapter 11. (J.A. 13a). The next day, on April 13, 1989, the bankruptcy court mailed a Notice for Meeting of Creditors, which set August 3, 1989, as the Bar Date for creditors to file a proof of claim. (J.A. 29a).

Mark Berlin, president of the corporate general partners of the Respondents (who were all creditors of Petitioner), received this Notice for Meeting and attended the first adjourned creditors' meeting. (J.A. 118a). Shortly thereafter, in early June, Respondents retained as counsel Marc Richards, an experienced bankruptcy practitioner, then with the New York law firm of Myerson & Kuhn. (J.A. 120a-21a; *see* J.A. 55a-58a). Mr. Berlin and Mr. Richards together attended the second meeting of creditors on June 16, 1989. (J.A. 119a).

Despite his receipt of the Notice for Meeting, his participation in both creditors' meetings, and Respondents' representation by Mr. Richards, Mr. Berlin was not aware of the necessity of filing proofs of claim by August 3, 1989. (J.A. 97a). Although he is an attorney, Mr. Berlin had no knowledge of bankruptcy practice, (J.A. 88a), was not acting in the capacity of counsel for Respondents, and did not understand the significance of the term "bar date." (J.A. 90a, 97a). Moreover, the Notice that the bankruptcy court sent to Mr. Berlin was not in the prescribed format of

Official Bankruptcy Form 16. The Court of Appeals for the Sixth Circuit observed that the Notice was a model of "dramatic ambiguity" -- even to an experienced bankruptcy practitioner. (J.A. 197a-98a). Mr. Richards himself did not recognize August 3 as a "bar date," (J.A. 57a), nor had he ever been aware of a case in which the deadline for filing proofs of claim was set so soon after the commencement of a significant chapter 11 case. (J.A. 58a).

In July 1989, Mr. Richards and his colleagues experienced ongoing difficulties with other attorneys at Myerson & Kuhn. As a result, Mr. Richards, three other bankruptcy partners, and virtually all of the bankruptcy associates resigned from Myerson & Kuhn effective July 31, 1989 (three days before the Bar Date in this case). (J.A. 56a). After his resignation, Mr. Richards was denied access to his files until August 15, 1989. *Id.* Even then, the file for this case was missing, and Mr. Richards was told that it could not be found. (J.A. 57a).

As a result, Respondents did not timely file proofs of claim. Twenty days after the August 3 Bar Date, Respondents moved the bankruptcy court under Bankruptcy Rule 9006 for an extension of time to file proofs of claim, based on their excusable neglect. (J.A. 31a). The bankruptcy court denied this motion for an extension of time. It held that the standard for showing excusable neglect permitted an extension only if the failure to act was based on circumstances beyond Respondents' reasonable control. (J.A. 128a).

Upon appeal by Respondents, the district court reversed and remanded, holding that the bankruptcy court had not correctly applied the "excusable neglect" standard set forth in Rule 9006. (J.A. 161a, 151a). The district court remanded for the bankruptcy court to determine whether there was excusable neglect by considering the factors specified in *In re Dix*, 95 Bankr. 134, 137 (Bankr. 9th Cir. 1988). (J.A. 158a-59a). On remand, the bankruptcy court again held that Respondents had not established excusable neglect. (J.A. 176a, 163a). The bankruptcy court foreclosed Respondents from filing their proofs of claim on the grounds that: (1) the delay in filing was within the reasonable control of Respondents and (2) because the filing was within their reasonable control, Respondents should be penalized for their counsel's neglect. (J.A. 169a-72a).

Respondents again appealed to the district court. This time the district court affirmed the bankruptcy court by simply holding that the bankruptcy court did not abuse its discretion in applying the factors specified in *Dix*. (J.A. 186a, 178a). Respondents then appealed to the Court of Appeals for the Sixth Circuit, which reversed. (J.A. 188a).

The Sixth Circuit held that the district court had applied an overly rigid analysis that failed to include the flexibility mandated by Rule 9006. (J.A. 195a). The bankruptcy court abused its discretion by unjustifiably penalizing Respondents for the neglect of their lawyer, (J.A. 198a), and by effectively rendering a default judgment

against Respondents, when there was no showing of any prejudice to Petitioner. (J.A. 198a-99a).

Petitioner's plan of reorganization has been confirmed and, significantly, it makes provision for the payment of Respondents' claims, should they be allowed. (J.A. 168a-69a). The plan proposes to pay unsecured creditors 100% of their claims. (Bankr. Ct. R. 3/27/90, pp. 6, 14).

SUMMARY OF ARGUMENT

Bankruptcy Rule 3003 directs the bankruptcy court to fix the time period for filing a proof of claim in a chapter 11 reorganization. The standard for allowing proofs of claim after the bar date is supplied by Rule 9006, which governs time limits generally, not just the time limit for filing proofs of claim. Rule 9006 authorizes the bankruptcy court to extend certain time periods, even after their expiration, based upon a showing of "excusable neglect."

This Court should affirm the Court of Appeals for the Sixth Circuit by adopting a flexible standard of "excusable neglect," which is required both by the plain language of Rule 9006 and the substantive policy of the Bankruptcy Code. Petitioner urges the application of a so-called "strict" standard. This proposed standard would preclude a finding of excusable neglect whenever the failure to act was within the party's reasonable control. This result is illogical and contrary to the plain meaning of Rule 9006, which expressly employs the term "neglect." Neglect, by definition, includes

the failure to perform an act that is within a party's control. If compliance with a deadline is within a party's reasonable control, then failure to comply with the deadline will almost always be due to neglect. Under Petitioner's proposed standard, however, the neglect will never be excusable for the very same reason.

A proper interpretation of excusable neglect requires a court to focus on whether the neglect is excusable. This necessarily involves a consideration of other factors than simply whether the failure to act was beyond the reasonable control of Respondents and their counsel. There is no uniform, rigid standard of excusable neglect under Bankruptcy Rule 9006, since neglect that may be excusable in one context may not be excusable in another.

In the context of Bankruptcy Rules 3003 and 9006, which deal with extending the date for filing proofs of claim in a chapter 11 reorganization, a court should guide its inquiry into whether neglect was excusable by considering whether the delay has caused any prejudice to the debtor or to other creditors, whether the delay has adversely impacted efficient judicial administration, and whether the creditor has acted in good faith. Only by undertaking such an inquiry can the courts' application of Rule 9006 properly reflect the *substantive* goals of the Bankruptcy Code -- preservation of claims and the avoidance of unjustified windfalls.

In this case, Respondents' neglect is excusable. The delay caused no prejudice to Petitioner or other creditors. The delay had no adverse impact on efficient judicial

administration. There is no question that Respondents acted in good faith. This Court should therefore affirm the conclusion of the Court of Appeals for the Sixth Circuit that the bankruptcy court erred by ignoring the proper meaning of "excusable neglect" so as to penalize Respondents for the neglect of their attorney.

ARGUMENT

I. "EXCUSABLE NEGLECT" PRESUMES THE EXISTENCE OF NEGLECT AND CANNOT, BY DEFINITION, BE LIMITED TO CIRCUMSTANCES BEYOND A PARTY'S REASONABLE CONTROL.

Two bankruptcy rules control this appeal. Bankruptcy Rule 9006(b)(1) provides generally for extensions of certain time periods. It covers not only time extensions for filing proofs of claim but, like Federal Rule of Civil Procedure 6(b), also governs virtually all other filing requirements (other than those that are expressly excluded). Rule 9006 requires a showing of "excusable neglect" where a party attempts to obtain an extension of time after the original time period has already expired. Bankruptcy Rule 3003 specifically governs the filing of proofs of claim in a chapter 11 case. It allows courts to extend the time for filing proofs of claim upon a showing of "cause." The two Rules must be read together. *Cf. Lujan v. National Wildlife*

Federation, 497 U.S. 871 (1990) (construing Federal Rules of Civil Procedure 6(b) and 56(c)).

In this case, the bankruptcy court held that "excusable neglect" could be shown only when the missed deadline was "beyond the reasonable control" of the party or its attorney. Under this rigid approach, the deadline for filing a bankruptcy proof of claim is treated almost like a statute of limitation, and equitable factors such as the good faith of the creditor, lack of prejudice to opposing parties, and lack of impact on efficient court administration may not be considered. The *only* relevant inquiry under this strict standard becomes whether the missed deadline was "beyond the reasonable control" of the party or its attorney.

This exclusive emphasis on conduct "beyond the reasonable control" of the moving party cannot be reconciled with the language of Rule 9006. Equating "excusable neglect" with circumstances "beyond the reasonable control" of a party is a logical *non sequitur* and violates the plain meaning of Rule 9006. The words "excusable neglect" in the Rule plainly presume that some type of neglect is involved. Obviously, if accomplishing an act is beyond one's reasonable control, then there is no neglect upon a failure to act. Rule 9006 by its terms allows relief for "neglect" -- the failure to take an act within one's control.[1/] The proper focus of a definition of "excusable neglect,"

[1/] *See, e.g.*, II Webster's Third New Int'l Dictionary 1513 (1971) (definition of neglect) ("to carelessly omit doing (something that should be done) either altogether or almost altogether: . . .").

therefore, necessarily includes omissions within a party's control. The correct focus of the inquiry is a consideration of whether any such neglect is "excusable."

The Third Circuit has recognized this principle in reviewing the decision of a district court that had denied an extension of time for filing a notice of appeal under Federal Rule of Appellate Procedure 4(a). *Consolidated Freightways Corp. v. Larson*, 827 F.2d 916, 918-19 (3d Cir. 1987), *cert. denied sub. nom.*, *Consolidated Freightways Corp. v. Secretary of Transportation*, 484 U.S. 1032 (1988). In *Consolidated Freightways*, the district court had interpreted Rule 4(a)(5) to establish a "*per se* rule that whenever counsel had, or should have had, 'control' over the underlying error, such error could not, as a matter of law, constitute excusable neglect." 827 F.2d at 918. The court of appeals rejected this illogical definition and held:

> We find it clear from the language of Rule 4(a) itself that the concept of excusable neglect encompasses more than acts, omissions, or events beyond the control of appellant and appellant's counsel. . . .
>
> By limiting applicability of the excusable neglect exception to errors beyond counsel's control, the district court ignored Rule 4(a)(5)'s purpose of excusing 'neglect.'

827 F.2d at 919.

The Third Circuit properly rejected the strict standard now advocated by Petitioner and held that "excusable

neglect" requires a case-by-case analysis. *Id.* Based on this interpretation, which is more logical and more faithful to the Rule's terms, the court compiled a list of factors to be considered in the analysis of "excusable neglect."[2/]

The excusable neglect standard in Bankruptcy Rule 9006 necessarily involves a determination of whether any neglect is excusable. That determination may vary according to the nature of the time extension requested. If excusable neglect were always defined by the rigid "beyond-the-reasonable-control" standard urged by Petitioner, then the trial court would have no discretion. The court would have to apply the strict standard rigidly and mechanically in every case, regardless of the length of the delay or the nature of the case. As the following section demonstrates, however, the excusable neglect standard is included in a variety of

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[2/] The court stated that the excusable neglect standard required weighing and balancing the following factors:

> (1) whether the inadvertence reflects professional incompetence such as ignorance of the rules of procedure;
> (2) whether the asserted inadvertence reflects an easily manufactured excuse incapable of verification by the court;
> (3) whether the tardiness results from counsel's failure to provide for a readily foreseeable consequence;
> (4) whether the inadvertence reflects a complete lack of diligence; or
> (5) whether the court is satisfied that the inadvertence resulted despite counsel's substantial good faith efforts toward compliance.

Consolidated Freightways, 827 F.2d at 919 (citations omitted).

other rules, and properly is interpreted flexibly according to the nature of the deadline for which an extension is sought.

Petitioner's advocacy of a rigid and mechanical application of Rule 9006 ignores the fact that Rule 9006 is only one of several rules that incorporates an excusable neglect requirement for obtaining time extensions. *See, e.g.*, Fed. R. Civ. P. 6(b), 13(f), *and* 60(b); Fed. R. App. P. 4(a); Bankr. R. 9033. Under some of these rules a flexible standard is called for; under others a strict standard may be more appropriate. A comparison of the standard of excusable neglect as it is applied in the context of these different rules reveals that "excusable neglect" serves different purposes, with appropriate strict deadlines for certain rules and more flexible deadlines for rules where discretion is appropriate.

Petitioner relies upon a selection of cases interpreting Federal Rule of Appellate Procedure 4(a). (Pet. Br. 24-25). While some courts have applied a strict approach to this jurisdictional deadline, they have done so for a reason that does not apply here. Under Federal Rule of Civil Procedure 73(a), which was the predecessor to Federal Rule of Appellate Procedure 4(a), excusable neglect could only arise where a party failed to learn of the entry of judgment. *Levisa Stone Corp. v. Elkhorn Stone Co.*, 411 F.2d 1208, 1210 (6th Cir. 1969), *cert. denied*, 397 U.S. 925 (1970). It is this particular pedigree of Rule 4(a) that has lead some courts to construe the excusable neglect standard narrowly as it applies to the filing of a notice of appeal. *See Reinsurance*

Co. v. Administratia Asigurarilor de Stat, 808 F.2d 1249, 1251 (7th Cir. 1987).

Contrary to the assertion in Petitioner's Brief that the Court of Appeals for the Sixth Circuit stands alone, courts often apply a flexible standard of excusable neglect in other contexts. For example, under Federal Rule of Civil Procedure 60(b), courts recognize a flexible standard of excusable neglect where consideration of the merits of a case would otherwise be foreclosed. *See, e.g., Augusta Fiberglass Coatings, Inc. v. Fodor Contracting Corp.*, 843 F.2d 808 (4th Cir. 1988). *Cf. In re Magouirk*, 693 F.2d 948, 951 (9th Cir. 1982) (recognizing flexible standard); *Livingston Powdered Metal, Inc. v. NLRB*, 669 F.2d 133, 136 (3d Cir. 1982) (recognizing flexible standard). That same consideration applies here, where Respondents risk losing their claim for reasons having nothing to do with its merits. When a party seeks a time extension on the basis of "excusable neglect," under general rules such as Federal Rule of Civil Procedure 6(b), the interpretation of excusable neglect also varies according to the nature of the extension being sought. Courts routinely -- and properly -- recognize the need for flexibility in granting short time extensions under these general rules where no bad faith or prejudice can be found. *See, e.g., Dominic v. Hess Oil V.I. Corp.*, 841 F.2d 513, 517 (3d Cir. 1988) (considering good faith under Fed. R. Civ. P. 6(b)); *In re Four Seasons Secs. Laws Litigation*, 493 F.2d 1288, 1290 (10th Cir. 1974)

(considering good faith and prejudice under Fed. R. Civ. P. 6(b)).

In many instances a party may miss a procedural deadline by only a few days. The opposing party would seldom object if no prejudice resulted. If Petitioner's inflexible and strict standard of excusable neglect were always appropriate, then the application of the standard could not vary according to the particular rule and the policy being served. An answer, routine motion, or a brief tendered even one day late could never be filed if it was within the reasonable control of the party to meet the filing deadline. The same would be true of all other filings governed by Bankruptcy Rule 9006 or the similarly worded Federal Rule of Civil Procedure 6(b). Petitioner's proposed standard would essentially convert a Rule mandating flexibility into one inviting imposition of default judgments as an everyday occurrence. Parties would reap financial windfalls from minor procedural defaults.

Like all overly harsh rules, this might promote certainty, but it was not the path chosen by the rule makers, who expressly provided that a party's neglect might be excusable. Application of Petitioner's standard in this case would result in a multi-million dollar windfall to Petitioner that is inconsistent with the policies served by the Bankruptcy Code and that would unduly restrict the discretion of the lower courts that must deal with the practical realities of litigation.

II. IN THE CONTEXT OF RULE 3003, "EXCUSABLE NEGLECT" SHOULD BE INTERPRETED FLEXIBLY.

Because the excusable neglect standard is a flexible one, the question before the Court in this case is how that standard should be applied in a chapter 11 case. In chapter 11 cases, the purposes of the Bankruptcy laws require that the proof of claim deadline not be construed rigidly and mechanically to promote default, as advocated by Petitioner. Rather, the deadline should be more flexibly construed in context by taking into account equitable factors that may excuse the neglect.

Petitioner, however, urges this Court to adopt a strict standard, citing in the abstract a need for certainty and finality. The fallacy in Petitioner's argument and the flaw in the cases upon which it relies is the failure to distinguish the needs and policy considerations in a chapter 11 reorganization case from those in a chapter 7 liquidation case. These important differences in context are reflected in the plain language of the different rules governing the filing of claims in each type of case.

A. Rule 3003 Allows a Time Extension Upon a Showing of Excusable Neglect, Unlike Rule 3002.

The difference between a claims deadline in a chapter 7 liquidation and a chapter 11 reorganization is readily seen by an examination of the plain language of Bankruptcy Rules

3002 and 3003. Except for certain narrow and specific exceptions, the Rule 3002 deadline for filing a chapter 7 proof of claim is absolute. In addition to the literal limitation of "within 90 days," the general standard of "excusable neglect" for late filings under Rule 9006(b) expressly does not apply to excuse a late-filed chapter 7 proof of claim. Bankr. R. 9006(b)(3).

On the other hand, the deadline for filing a chapter 11 proof of claim is much less restrictive. Bankruptcy Rule 3003(c), unlike Rule 3002(c), expressly allows the deadline for filing a chapter 11 proof of claim to be extended "for cause shown." Thus, although a chapter 7 creditor may not obtain a post-deadline extension of time unless it is within one of the narrow specified exceptions to rule 3002(c), a chapter 11 creditor may obtain an extension of time upon a showing of "cause" or "excusable neglect." *See* 8 King, *Collier on Bankruptcy* ¶ 3003.05[4][a] (15th ed. 1989) ("Unlike Rule 3002, Rule 3003(c) does not set up a statute of lin s leaving the court with no discretion to allow late file aims.").

The bankruptcy court's error, which Petitioner urges this Court to repeat, is highlighted by its failure to distinguish the deadline for a chapter 7 proof of claim from a deadline for a chapter 11 proof of claim:

> Under the extreme facts of this case, a finding that the partnerships' claims should be allowed as timely filed would establish a precedent difficult to overcome in Chapter 11 and Chapter 7 asset cases.

(J.A. 173a). As can be seen from the above analysis of the bankruptcy rules, however, precedents set in chapter 11 cases cannot govern in chapter 7 cases. This analytical error not only misled the bankruptcy court in this case, but also is at the heart of the other cases upon which Petitioner relies. As discussed below, the various court of appeals decisions relied upon by Petitioner and by the bankruptcy court fail to distinguish between the strict chapter 7 deadline and the more flexible chapter 11 deadline.

B. The Authorities Cited by Petitioner Fail to Distinguish Chapter 11 from Chapter 7.

The major underpinning of Petitioner's argument is four opinions from circuit courts that have adopted the so-called strict standard. *In re Vertientes, Ltd.*, 845 F.2d 57 (3d Cir. 1988); *Maressa v. A.H. Robins Co.*, 839 F.2d 220 (4th Cir.), *cert. denied*, 488 U.S. 826 (1988); *In re South Atlantic Fin. Corp.*, 767 F.2d 814 (11th Cir. 1985), *cert. denied sub. nom., Biscayne 21 Condominium, Inc. v. South Atlantic Fin. Corp.*, 475 U.S. 1015 (1986); *Hoos & Co. v. Dynamics Corp.*, 570 F.2d 433 (2d Cir. 1978). These cases, however, are not well-reasoned. They involve chapter 11 filings, but their analysis improperly relies upon decisions that interpret Bankruptcy Rule 3002 or other rules that (unlike Bankruptcy Rule 3003) do not permit late, discretionary extensions of time for excusable neglect.

Vertientes, for example, relied heavily upon *In re Pigott*, 684 F.2d 239 (3d Cir. 1982) for the principle that a

bankruptcy court cannot weigh equitable considerations to allow untimely claims. 845 F.2d at 60. *Pigott*, however, was decided under a different statute, 11 U.S.C. § 57(n) and former Rule 302(e). Unlike Rule 3003, both that statute and rule provided for an extension of time *only* if a request for additional time was made prior to the expiration of the time period. 684 F.2d at 242 nn.1, 2. Former Rule 906(b) also expressly excluded Rule 302(e) from use of the general standard of "excusable neglect." *Id.* Thus, in *Pigott* no equitable factors could be considered because there was no provision in the statute or in the rule for post-deadline motions for extension of time. *Vertientes'* reliance on *Pigott* therefore was misplaced because Bankruptcy Rule 3003(c) -- unlike former Rule 302 and unlike present Rule 3002(c) -- specifically gives the bankruptcy court the discretion to consider a post-deadline motion for extension of time in a chapter 11 case.

In addition to *Pigott*, the *Vertientes* court also relied upon three other cases for the principle that equitable factors should not be considered in granting or denying a time extension. All of these underlying cases, however, were based on Rule 3002 or former rules that, unlike Rule 3003, did not permit extensions of time or even motions for extension of time after the expiration of the proof of claim deadline: *In re Stern*, 70 Bankr. 472, 474-75 (Bankr. E.D. Pa. 1987) (applied non-discretionary deadline under Rule 3002); *In re Owens*, 67 Bankr. 418, 423 (Bankr. E.D. Pa. 1986) (applied non-discretionary deadline under Rule 3002),

aff'd, *United States v. Owens*, 84 Bankr. 361 (E.D.Pa. 1988); *In re Supernit*, 186 F.2d 130, 132 (3d Cir. 1950) (applied non-discretionary deadlines under former § 355 of the Bankruptcy Act). Thus, while all the cases underpinning *Vertientes* may have been sound in their own particular context, they do not support the result in *Vertientes*; nor do they support the notion that excusable neglect under Bankruptcy Rule 9006 does not involve the consideration of equitable principles.

The one-page *Maressa* opinion quoted the principle of finality stated in *Hoos & Co. v. Dynamics Corp.*, 570 F.2d 433 (2d Cir. 1978). *Maressa*, 839 F.2d at 221. *Hoos*, however, also involved a rule that expressly excluded late extensions of time. *See Hoos*, 570 F.2d at 437-39 (applied non-discretionary deadline of former Rule 11-33(b)(2)). As in *Pigott*, the rule did not provide for a post-deadline motion seeking an extension of time and was expressly excluded from former Rule 906(b). *Id.* *Hoos* therefore has no application to the discretionary standard under rule 3003(c) in a chapter 11 case and provided no support for *Maressa*, which itself therefore provides no foundation for Petitioner's argument. Finally, *South Atlantic* suffers from the same deficient analysis. It too relied heavily on cases construing

rules that, unlike Bankruptcy Rule 3003, do not permit post-deadline filings. *See* 767 F.2d at 814.[3]

In short, the circuits that have adopted the so-called strict view of excusable neglect in the context at issue here have done so based upon a flawed and incomplete analysis. This Court therefore should reject their inflexible approach and adopt the discretionary approach that permits a consideration of factors such as good faith, lack of prejudice to other parties, and the lack of adverse impact on judicial administration.

C. The Purposes of Bankruptcy Law Require a Flexible Standard of Excusable Neglect in Chapter 11 Cases.

The present Advisory Committee notes to Rule 3003(c) demonstrate that extensions under that Rule should be liberally granted to preserve rather than to forfeit rights. Present Bankruptcy Rule 3003 is adapted from former Chapter X Rule 10-401. *See* Rule 3003 Advisory Committee note. The Advisory Committee notes for the former rule demonstrate that its drafters intended that equitable factors be considered in granting time extensions to creditors who neglect to file claims on time. Because present Bankruptcy

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[3] Petitioner's reliance on this Court's opinion in *United States* v. *Locke*, 471 U.S. 84 (1985) suffers from the same flaw. That case involved deadlines under the Federal Land Policy and Management Act of 1976, 43 U.S.C. § 1744, which did not contain a discretionary excusable neglect standard for time extensions.

Rule 3003 is adapted from this former rule, this history is germane to a proper interpretation of the current rule.

The Advisory Committee notes for former Rule 10-401 explained the purpose served by the rule:

> If the court has fixed a bar date for the filing of proofs of claim, it may still enlarge that time within the provisions of Bankruptcy Rule 906(b) which is made applicable in this subdivision. *This policy is in accord with Chapter X generally which is to preserve rather than to forfeit rights.* [I]t rejects the notion expressed in § 57n of the Act that claims must be filed within a six-month period to participate in any distribution. . . . This approach was intentional as expressed in Senate Report 1916 (75th Cong., 3d Sess., April 20, 1938):
>
> > Sections 204 and 205 insure participation in the benefits of the reorganization to those who, *through inadvertance or otherwise*, have failed to file their claims or otherwise evidence their interests during the pendency of the proceedings.
>
> This attitude is carried forward in the rules, first by dispensing with the need to file proofs of claim . . . in most instances and, secondly, by permitting enlargement of the fixed bar date in a particular case with leave of court and for cause shown *in accordance with the equities of the situation.*

Former Rule 10-401 Advisory Committee note (emphasis added), *reprinted in* 2 King, *Bankruptcy Act and Rules* 1084 (1976 Pamphlet Ed.).

Thus, in a chapter X case, the setting of a claims deadline was for the purpose of preserving rather than forfeiting rights with the granting of an enlargement of time consistent with the "equities of the situation." *Id.* The notes specifically distinguish § 57n which required a filing within six months of the first creditor's meeting. Section 57n was the predecessor of the current 90-day deadline for chapter 7 cases set in Rule 3002(c). *In re Stern*, 70 Bankr. 472, 475 (Bankr. E.D. Pa. 1987). Accordingly, the chapter 11 deadline in Rule 3003(c), as adapted from former Rule 10-401, should also be interpreted to preserve creditors' rights and not automatically to eliminate claims that are tendered after the deadline through inadvertence or otherwise.

D. Proper Analysis of "Excusable Neglect" Involves Consideration of Three Equitable Factors.

The purpose of a filing deadline in a chapter 11 case is to allow the debtor to estimate its potential liabilities so that it can formulate a plan of reorganization. *See In re Chicago Rock Island & Pac. R.R.*, 788 F.2d 1280, 1281 (7th Cir. 1986). This filing deadline is most important when the debtor is in the process of preparing its plan. Obviously, the debtor's ability to formulate a feasible plan is dependent upon what it perceives to be the extent of its liabilities. If

major creditors were routinely permitted to file proofs of claim at any time after the debtor's disclosure statement and proposed plan of reorganization are filed, then the debtor would be forced to amend its plan and disclosure statement or even conclude that reorganization is not feasible. Any resulting delay would also adversely impact efficient court administration. On the other hand, promoting the need for finality through the rigid and arbitrary approach advanced by Petitioner would sacrifice the bankruptcy goals of preserving valid claims and preventing unjustified windfalls.

These competing concerns have been reconciled in the approach taken by the Sixth Circuit in this case and two other courts of appeal that have looked to equitable factors in evaluating claims of excusable neglect. *See In re Dix*, 95 Bankr. 134 (Bankr. 9th Cir. 1988) (Rule 9006); *Consolidated Freightways Corp. v. Larson*, 827 F.2d 916 (3d Cir. 1987) (Fed. R. App. P. 4(a)) (subsequent history omitted). While these courts have applied different labels and different numbers of factors, three considerations lie at the heart of this flexible approach.[4] Respondent submits that these factors are: (1) whether there is prejudice to the debtor or other creditors; (2) the length of the delay and its

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[4] In *Dix*, the court also recognized as a factor to be considered whether "the delay was beyond the reasonable control of the person whose duty it was to perform." 95 Bankr. at 138. As discussed throughout this Brief, this test cannot be used as the sole inquiry in evaluating excusable neglect as Petitioner urges. Nonetheless, Respondent agrees that a finding that the delay was beyond the control of the late-filing party likely establishes that relief is appropriate.

impact on efficient court administration; and (3) whether the creditor acted in good faith. *See Dix*, 95 Bankr. at 138; *Consolidated Freightways*, 827 F.2d at 919. Various specific considerations may fall under each of these headings, and the names of the factors themselves might easily be rephrased. The important point, however, is that these are the three substantive considerations that Respondent submits should guide this Court in fashioning a standard for determining excusable neglect.

The application of these factors will necessarily vary depending on the facts of the situation. For example, even if a creditor has acted in good faith, significant prejudice to the debtor in redrafting or even scrapping its proposed plan of reorganization or a detrimental effect on court administration may require a denial of a motion for an extension of time. This might be the case in a small reorganization involving limited assets and a small number of creditors where the debtor may be able to begin formulating a plan immediately upon the filing of its petition.

In a large, complex bankruptcy case such as this one, however, the debtor may not begin formulating a plan for several months. In fact, Petitioner did not file a proposed plan and disclosure statement until January 2, 1990, over four months after Respondents tendered their proofs of claim. This plan and disclosure statement went through several modifications after discussions with various creditors, including Respondents, resulting in the approval of an amended disclosure statement in April 1990. *See* (J.A.

169a). Thus, as the bankruptcy court found, no prejudice resulted because Petitioner had not begun formulating its plan when Respondents' proofs of claim were tendered, because the filing of the claims did not interfere with Petitioner's ability to formulate its plan, and because the plan specifically makes provision for the allowance of Respondents' claims.

In this case, the Sixth Circuit followed *Dix*, but held that its list of equitable considerations was not exclusive. (J.A. 195a-96a). Thus, it also weighed the absence of culpable conduct on the part of Respondents and weighed the policy of hearing claims on their merits, rather than using default judgments to discipline attorneys. (J.A. 198a-99a). Of course, the factor denominated as "culpable conduct" by the Sixth Circuit might just as easily fit under the heading of "good faith." And attention to furthering the policy of deciding cases on the merits is always appropriate. But whatever titles are given to the relevant factors, the Sixth Circuit was manifestly correct when it concluded that the bankruptcy court applied an incorrect legal standard by placing undue emphasis on whether the admitted neglect was "beyond the reasonable control" of Respondents or their counsel.

III. RESPONDENTS HAVE DEMONSTRATED "EXCUSABLE NEGLECT" AND SHOULD BE ALLOWED TO FILE THEIR PROOFS OF CLAIM.

A. The Bankruptcy Court and Court of Appeals Correctly Found that the Relevant Factors Favor Respondents.

A principled application of these flexible factors compels the conclusion that Respondents' neglect was indeed "excusable." As the court of appeals held, (J.A. 198a), the bankruptcy court correctly resolved all these factors in favor of Respondents. (J.A. 198a). Petitioner does not contest these findings here. *See also, e.g., Goodman v. Lukens Steel Co.*, 482 U.S. 656, 665 (1987) (under two-court rule, this Court accepts trial court findings affirmed by court of appeals).

Weighing the first factor, prejudice to Petitioner, the bankruptcy court found that Petitioner "will not be prejudiced by granting the filing of [Respondents'] motion beyond the August 3, 1989 bar date." (J.A. 169a). This conclusion stands unchallenged on appeal; no prejudice to Petitioner or to other creditors results from granting Respondents' motion to permit filing of the proofs of claim. Moreover, Petitioner's plan makes provision for payment of Respondents' claims if they are allowed. (J.A. 168a-69a).

The bankruptcy court also correctly resolved the second factor, which considers the impact on efficient court

administration, in favor of Respondents. "[T]he [20 day] delay has had no adverse or negative impact on efficient court administration." (J.A. 169a).

The bankruptcy court also resolved the third factor, good faith, in favor of Respondents. The court found "nothing in the record to suggest that [Respondents] or their former attorney, Marc Richards, acted other than in good faith in the filing of [Respondents'] claims." (J.A. 170a).

Therefore, the bankruptcy court concluded that Respondents had caused no prejudice to Petitioner, had acted in good faith, and had not adversely impacted efficient court administration due to the short delay. These conclusions of the bankruptcy court are not questioned; they are not at issue before this Court. The Sixth Circuit's decision should therefore be affirmed.

B. Whether Respondents Should Be Penalized for the Neglect of their Counsel Is Not a Factor in Determining Excusable Neglect.

The bankruptcy court refused to permit the filing of Respondents' proofs of claim, holding that Respondents should be penalized for the neglect of their attorney Richards, (J.A. 172a), simply because Mr. Berlin had received the Notice for Meeting of Creditors. (J.A. 171a). It did so by placing undue emphasis on the propriety of "penalizing" the neglect of counsel, a fourth factor that had been applied in the Ninth Circuit Bankruptcy Panel's *Dix* opinion. The bankruptcy court's reasoning, however, would

always preclude a finding of excusable neglect whenever a client had notice of a deadline.[2/] This demonstrates this fourth factor should not be an independent consideration at all.

Respondents recognize that, as a general rule in our representative system of litigation, the client is bound by the acts and omissions of its counsel. *Link v. Wabash R.R.*, 370 U.S. 626, *reh'g denied*, 371 U.S. 873 (1962). But it does not follow from this that the client *always* must be penalized for the negligence of its counsel. If the neglect of counsel is excusable under the flexible factor approach, then the client need not be penalized. There is no reasoned basis for concluding, as did the bankruptcy court, that this should be an overriding factor in determining whether the neglect is excusable in the first instance.

[2/] The bankruptcy court concluded that the fact that Mr. Berlin had actual knowledge of the bar date "precludes the court from finding that it would be improper to penalize [Respondents] for the neglect of their attorney." (J.A. 172a). But the appropriate factors already account for this situation by focusing on the bad faith of the attorney or the party. In this case, finding it appropriate to penalize the party for the attorney's misconduct on the mere basis of his knowledge of the bar date is nothing more than a reworded application of the "beyond the reasonable control" standard. If penalizing improper conduct is to be an independent factor, it must be for some *further* misconduct on the part of the attorney or party. Any such situation, however, is already encompassed within the flexible approach Respondents propose to this Court, which includes attention to "bad faith." In this case, the bankruptcy court correctly concluded that there was *no* bad faith on the part of Respondents or their attorney.

In *Link*, the primary case relied upon by Petitioner, the Court held that a federal district court has the power and authority under Federal Rule of Civil Procedure 41 to dismiss a case, *sua sponte* and with prejudice, for a plaintiff's failure to prosecute. *Link*, 370 U.S. at 629. The *Link* Court did observe that, as the result of such a dismissal, the client certainly would suffer because of the negligence and indifference of its counsel. The *Link* Court itself, however, expressly recognized that the aggrieved client could have utilized the "escape hatch" of Rule 60(b) of the Federal Rules of Civil Procedure to avoid being penalized for the neglect of its attorney. *See* 370 U.S. at 632. Significantly, the "escape hatch" to which *Link* referred was the district court's power to set aside a judgment that resulted from excusable neglect, thus implicitly recognizing that a client could avail itself of excusable neglect to avoid the consequences of attorney negligence.[9]

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[9] *Link* certainly does not hold that an attorney's neglect must *always* be used to penalize his client, and Petitioner's broad statement that the sins of the attorney must *always* be visited upon the client obviously is overbroad in light of the many express provisions under which the attorney, and not the client, is penalized for conduct during litigation. *See, e.g.*, 28 U.S.C. § 1927 (attorney liable for costs of vexatious litigation). *Cf.* Fed. R. Civ. P. 11; *Business Guides, Inc. v. Chromatic Communications Enters.*, 111 S. Ct. 922 (1991) (client not liable for Rule 11 sanctions if client himself does not sign filed papers).

Petitioner also cites *United States v. Boyle*, 469 U.S. 241 (1985), for the proposition that reliance on an attorney cannot ever constitute excusable neglect. *Boyle*, however, only holds that under certain circumstances a taxpayer cannot assert that reliance on counsel constitutes the "reasonable cause" that 26 U.S.C. § 6651(a)(1) requires to avoid statutory penalties for filing a tax return late. The *Boyle* Court made no attempt to define the contours of an entirely different standard -- excusable neglect -- in an entirely different context -- the Bankruptcy Code. Moreover, the *Boyle* holding is limited by the unique aspects of our "self-assessment" system of taxation. *See* 469 U.S. at 249. Every taxpayer reasonably may be charged with knowledge of the duty to comply with filing deadlines for tax returns; the *Boyle* Court noted that this duty to file tax returns is a non-delegable duty. *Id.*

This Court also recognized an exception in *Boyle* that a taxpayer's reliance upon professional advice may constitute "reasonable cause" for failure to meet the filing deadline. 469 U.S. 250 (citing *Commissioner v. Lane-Wells Co.*, 321 U.S. 219 (1944); *Haywood Lumber & Mining Co. v. Comm'r*, 178 F.2d 769, 771 (2d Cir. 1950) and other authorities). Were *Boyle* applicable here, this exception would apply. In this case, Mr. Berlin specifically asked his attorney, Mr. Richards, about the time for filing the proofs of claim and was erroneously told that "as there was no bar date, that the filing of [Respondents'] proofs of claim was not a matter of urgency." (J.A. 121a). Reliance upon

counsel in this specialized area of the law distinguishes this case from *Boyle* and illustrates the inequity of entering what is effectively a multi-million dollar default judgment against Respondents based solely on the neglect of their counsel.

Therefore, in determining whether neglect is excusable, this Court should adopt a flexible approach that weighs the impact on efficient court administration, that considers whether there is prejudice to the debtor or other creditors, and that takes into account the good faith of the creditor. Given the findings already made on these factors below, this Court should order that Respondents' proofs of claim be filed.

CONCLUSION

The decision of the Court of Appeals for the Sixth Circuit permitting Respondents to file their proofs of claim should be affirmed.

Respectfully submitted,

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